Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of	)	
	)	
Implementation of Section 301(j) of the	)	
Telecommunications Act of 1996	)	CS Docket No. 96-57
	)	
Aggregation of Equipment Costs	)	
By Cable Operators	)	
	)	

REPORT AND ORDER

Adopted: June 6, 1996 **Released: June 7, 1996**

By the Commission:

I. INTRODUCTION

1. In this *Report and Order*, we amend our rules to implement Section 301(j) of the Telecommunications Act of 1996 ("1996 Act"),[1] which adds a new Section 623(a)(7) to the Communications Act of 1934, as amended ("Communications Act").[2] Section 301(j) of the 1996 Act requires that "[t]he Commission allow cable operators to aggregate, on a franchise, system, regional, or company level, their equipment costs into broad categories regardless of the varying levels of functionality of the equipment within each such broad category."[3] That section also provides that "[s]uch aggregation shall not be permitted with respect to equipment used by subscribers who receive only a rate regulated basic service tier."[4]

2. The amended rules contained herein are designed to reflect the Congressional intent to promote the development of a broadband, two-way telecommunications

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[1] Pub. L. No. 104-104, 110 Stat. 56, 118 (1996).

[2] Communications Act, § 623(a)(7)(A), 47 U.S.C. § 543(a)(7)(A).

[3] *Id.*

[4] *Id.*

infrastructure.[5] Furthermore, we believe that these amended rules will reduce the cost of advanced technology for consumers and permit manufacturers to more easily implement future technical innovation in the broadband industry. Finally, these amended rules should ease the burden of cable rate regulation on operators and prove more administratively efficient for both local franchising authorities and cable operators.

II. BACKGROUND

3. In *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992; Rate Regulation, Report and Order and Further Notice of Proposed Rulemaking*, MM Docket No. 92-266 ("*Rate Order*"),[6] the Commission established rules to implement the cable television rate regulation provisions of the Cable Television Consumer Protection and competition Act of 1992 ("1992 Cable Act"). The 1992 Cable Act requires that rates for equipment and installations be based on actual costs.[7] The 1992 Cable Act and the rules promulgated in the *Rate Order* provide for regulation of the basic service tier by local franchising authorities, pursuant to rules promulgated by the Commission,[8] and of the cable programming services tier by the Commission upon the filing of a complaint.[9] Rates for equipment used to receive residential cable service generally are regulated by the local franchising authority pursuant to rules promulgated by the Commission.[10]

4. With respect to aggregating equipment by categories, the Commission's current rules require separate charges for each "significantly different" type of remote, converter box, and other customer equipment.[11] For example, a cable operator that offered two significantly

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[5] *See* H.R. Rep. 204, 104th Cong., 1st Sess. at 107 ("House Report"); *see also* Conf. Rep. 104-230, 104th Cong, 2d Sess. at 167.

[6] 8 FCC Rcd 5631 (1993).

[7] Communications Act, § 623(b)(3), 47 U.S.C. § 542(b)(3).

[8] The basic service tier must include: (1) all local commercial and noncommercial educational television and qualified low power station signals carried to meet carriage obligations imposed by Sections 614 and 615 of the Communications Act; (2) any public, educational, and governmental access programming required by the franchise to be provided to subscribers; and (3) any signal of any television broadcast station except a signal that is secondarily transmitted by a satellite carrier beyond the local service area of such a station. Communications Act, § 623(b)(7)(A), 47 U.S.C. § 543 (b)(7)(A).

[9] A cable programming service is "any video programming provided over a cable system, regardless of service tier, including installation or rental of equipment used for the receipt of such video programming, other than (A) video programming carried on the basic service tier, and (B) video programming offered on a per channel or per program basis." Communications Act, § 623(1)(2), 47 U.S.C. § 543(1)(2).

[10] *See* 47 C.F.R. §§ 76.922-76.923, 76.944-76.945.

[11] 47 C.F.R. §§ 76.923(f), (g).

different types of remotes would have two different rates for remotes. Installation charges are based on the hourly service charge multiplied either by the actual time spent on each individual installation or by the average time spent for each specific type of installation.[12] The hourly service charge is a component in the calculation of customer equipment rates.[13]

5. With respect to aggregating equipment on organizational levels, cable operators are currently permitted to aggregate costs at the franchise, system, regional, and/or company level, but if they do so, only in a manner consistent with the accounting practices of the operator on April 3, 1993.[14] Further, the Commission's rules already permit small system operators to average their equipment costs at any level, regardless of the operator's practices as of April 3, 1993, subject to safeguards designed to protect subscribers from unusual rate changes.[15] This has reduced the administrative burdens associated with setting unbundled equipment rates based on actual costs. Our rules have only permitted this flexibility for equipment costs, however, not for installation charges.[16] This was done because we believed that equipment charges were less likely to vary significantly between systems, whereas installation charges are more dependent on local labor and other costs that can vary among communities.[17]

6. On March 20, 1996, pursuant to Section 301(j) of the 1996 Act, we adopted a Notice of Proposed Rule Making[18] to carry out the requirements of Section 301(j), proposing

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[12] 47 C.F.R. § 76.923(e).

[13] Specifically, customer equipment rates are calculated as follows:

$$\text{Monthly Charge} = \frac{\text{UCE} + (\text{HSC} \times \text{HR})}{12}$$

UCE = average annual unit cost of the equipment. HSC = an operator's annual Equipment Basket costs, excluding the purchase cost of customer equipment, divided by the total person hours involved in installing, repairing and servicing customer equipment during the same period. HR = average hours repair per year. *See* 47 C.F.R. §§ 76.923(f), (g). The Equipment Basket includes all costs associated with providing equipment and installations, including a reasonable profit. 46 C.F.R. § 76.923(c).

[14] 47 C.F.R. § 76.923(c).

[15] 47 C.F.R. § 76.923(l). Second Order on Reconsideration, Fourth Report and Order, and Fifth Notice of Proposed Rulemaking in MM Docket 92-266, (*"Benchmark Order"*) FCC 94-38, 9 FCC Rcd 4119 (1994). This approach allowed small system operators to base equipment rates on actual costs and average those costs at an organizational level selected by the operator.

[16] *Benchmark Order*, 9 FCC Rcd at 4220.

[17] *Benchmark Order*, 9 FCC Rcd at 4227-28.

[18] Implementation of Section 301(j) of the Telecommunications Act of 1996 , CS Docket No. 96-57, *Notice of Proposed Rule Making*, __ FCC Rcd ___ (1996) (*"Notice"*).

changes to our rules to minimize administrative and regulatory burdens associated with setting equipment rates under our rules. Section 301(j) of the 1996 Act amends Section 623(a) of the Communications Act by adding the following subsection (7):

> (7) Aggregation of Equipment Costs
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> (A) In General - The Commission shall allow cable operators, pursuant to any rules promulgated under subsection (b)(3), to aggregate, on a franchise, system, regional, or company level, their equipment costs into broad categories, such as converter boxes, regardless of the varying levels of functionality of the equipment within each such broad category. Such aggregation shall not be permitted with respect to equipment used by subscribers who receive only a rate regulated basic service tier.
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> (B) Revision to Commission Rules; Forms - Within 120 days of the date of enactment of the Telecommunications Act of 1996, the Commission shall issue revisions to the appropriate rules and forms necessary to implement subparagraph (A).

In response to our *Notice*, we received several comments and reply comments from interested parties.[19]

III. DISCUSSION

A. Equipment Categorization

7. *Background.* In the *Notice*, we indicated that we believed the intent of Section 301(j) is to permit operators to classify and to place equipment in broad categories based on the equipment's primary purpose.[20] We therefore proposed to amend the Equipment Basket provisions in Section 76.923(c) to allow categorization of customer equipment costs into broad categories based on its primary purpose.[21] We further proposed eliminating the language in Sections 76.923(f) and (g) that requires separate charges for each significantly different type of remote control device, converter box, and other customer equipment.[22] We proposed eliminating Section 76.923(l) of our rules, which permits small systems to aggregate costs for "similar types of equipment" on a company-wide basis, since all operators will be

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[19] The parties that filed comments in this proceeding are: the National Cable Television Association ("NCTA"); Time Warner Cable ("Time Warner"); Tele-Communications , Inc. ("TCI"); General Instrument Corporation ("General Instrument"); Telecommunications Industry Association ("TIA"); the New York State Department of Public Service ("New York PSC"); and the State of New Jersey Division of the Ratepayer Advocate ("New Jersey Rate Advocate"). Time Warner, General Instrument and TIA filed reply comments.

[20] *Notice* _ FCC Rcd at __, ¶ 8.

[21] *Notice*, __ FCC Rcd at __, ¶ 9.

[22] *Notice*, __ FCC Rcd at __, ¶ 9.

permitted to aggregate such costs under the 1996 Act.[23] Finally, we tentatively concluded that equipment associated with the installation of initial and additional connections could not be aggregated into a broad category.[24] We sought comment on our tentative conclusions, proposed rule amendments and whether defining the term "level of functionality" used in the 1996 Act would bring more certainty to these rules.[25]

8. *Discussion.* We conclude that Congress intended to permit operators to aggregate equipment costs into broad categories, limited only by the requirement that equipment so aggregated be of the same type.[26] We amend the Equipment Basket provisions in Section 76.923(c) to allow categorization of customer equipment costs into broad categories. Furthermore, because it would prevent the broad categorization intended by Congress, we eliminate the language in Sections 76.923(f) and (g) that requires separate charges for each significantly different type of remote control device, converter box and other customer equipment.

9. The "primary purpose" test, proposed in the *Notice*, for categorizing equipment will not be used, nor will it be incorporated into our rules. Instead, equipment may be categorized together if of the same type. Though all parties that filed comments in this proceeding support our proposed broad categories test, some were concerned that classifying equipment based on its primary purpose would create uncertainty and cause disputes as to what was the primary purpose of multi-function equipment.[27] Moreover, those parties asserted that attempting to determine the primary purpose of a piece of equipment is similar to an inquiry into the "functionality" of the equipment, an inquiry specifically prohibited by the statute.[28] Instead, those parties state that operators should be permitted to aggregate equipment costs into broad categories as long as the equipment is of the same type.[29] We agree and amend our rules accordingly. By specifying converter boxes as an example of an appropriate category, Congress indicated its intent that the broad categories into which equipment could be grouped were by type of equipment. The New Jersey Rate Advocate believes that "level of functionality" should be defined in order to limit the categorization of

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[23] *Notice*, __ FCC Rcd at __, ¶ 9.

[24] *Notice*, __ FCC Rcd at __, ¶ 10.

[25] *Notice*, __ FCC Rcd at __, ¶ 9.

[26] Also, as discussed below, we conclude that Congress did not intend the costs of equipment used by basic-only subscribers to be aggregated with the costs of equipment used by other subscribers.

[27] NCTA Comments at 5-6; Time Warner Comments at 2-3; TCI Comments at 6-8; General Instrument Comments at 7-8; TIA Comments at 3.

[28] *Id.*

[29] *Id.*

costs to those elements of customer equipment that provide common functionality.[30] For example, the New Jersey Rate Advocate believes that addressable and non-addressable converters contain two levels of functionality and should therefore not be categorized together.[31] The New Jersey Rate Advocate's position is inconsistent with language in the 1996 Act that explicitly permits operators to establish a broad category for converter boxes without regard to level of functionality. We therefore see no need to define level of functionality further in our rules.

10. Under the revised rules adopted herein, there are three types of customer equipment: converter boxes, remote controls and inside wiring.[32] Current customer equipment costs should therefore be aggregated into one of these categories. We will maintain a flexible approach with respect to categorization of new technology. For example, when new types of advanced boxes are designed and developed for use in cable systems, operators may broaden the "converter box" category and aggregate such new technology with other boxes that are used to receive services delivered over the cable system, notwithstanding the fact that the new equipment may perform other functions as well.

11. Several parties asked the Commission to clarify that operators have the flexibility to average some equipment of the same type, but not all equipment of that type.[33] For example, NCTA stated that operators should be permitted to average addressable analog boxes with digital boxes, without also having to include standard, non-addressable analog boxes in that averaging process.[34] We agree. The 1996 Act directs the Commission to "allow," not force, operators to aggregate costs into broad categories. In other words, operators may choose how broadly to categorize equipment if they choose to do so at all. We note that Section 301(j) simply permits, but does not require, an operator to aggregate equipment costs.

12. Though we tentatively concluded otherwise in the *Notice*, we will not eliminate Section 76.923(l) of our rules, which permits cost aggregation specifically for smaller cable systems.[35] In prescribing regulations under Section 301(j), we must be mindful of Section 623(i) of the Communications Act which directs the Commission, in developing and

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[30] The New Jersey Rate Advocate Comments at 4-6.

[31] *Id.* at 4-5.

[32] *See* 47 C.F.R. § 76.923(a).

[33] NCTA at 5; Time Warner Comments at 2-3; General Instruments at 5-6.

[34] NCTA Comments at 5.

[35] Our rules for smaller cable systems permit cost aggregation even for equipment used by subscribers who receive only the basic service tier. *See* 47 C.F.R. § 76.923(l).

prescribing regulations pursuant to Section 623,[36] to design such regulations to reduce the administrative burdens and cost of compliance for smaller cable systems.[37] We conclude that Section 76.923(l) of our rules with respect to smaller cable systems should not be eliminated, since doing so might increase administrative burdens and cost of compliance on smaller cable systems, the concerns Congress directed us to guard against in section 623(i) of the Communications Act.[38]

13. In the *Notice*, we tentatively concluded that costs of equipment used in the installation of initial and additional outlets could not be aggregated into a broad category. Several parties disagreed with our tentative conclusion and asked the Commission to clarify that although separate installation rates for initial and additional outlets will still be required under our proposed rule changes, equipment costs associated with such installations may nevertheless be aggregated into the same broad category.[39] We now do so. While Section 623(b)(3) of the Communications Act, upon which we based our tentative conclusions, requires that rates for initial cable installation as well as installation of connections for additional television receivers be separate and based on actual cost, it does not preclude aggregation of equipment costs associated with installation.[40] The only equipment used for the installation of both initial and additional outlets is inside wiring, including splitters and signal boosters needed occasionally with additional outlets. To prohibit operators from aggregating costs of the inside wiring into a broad category would frustrate Congress' intent in passing the equipment cost aggregation provision, Section 301(j) of the 1996 Act. We shall therefore amend our rules to clarify that equipment costs associated with both initial connections and additional outlets, including splitters and signal boosters, may be aggregated into one broad category. Installation charges and monthly use charges for both outlets are unaffected by this rule change, which simply relates to equipment costs. The New Jersey Rate Advocate stated, without argument, that equipment costs for initial and additional outlets should not be permitted to be aggregated into the same category.[41] As explained above, because the equipment used for both procedures is of the same type, i.e., inside wiring, we

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[36] Section 301(j) of the 1996 Act is Section 623(a)(7) of the Communications Act.

[37] Communications Act, § 623(i); *see* 47 C.F.R. § 76.923(l); *see also* 47 C.F.R. § 76.901(c).

[38] Moreover, Congress explicitly provided for greater deregulation for small cable companies in the 1996 Act. *See* 1996 Act, § 301(c); Communications Act, § 623(m). For example, the 1996 Act provides that in any franchise area in which a small cable operator serves fewer than 50,000 subscribers, our rate regulations no longer apply to the cable programming services tier. *Id.* In some instances, such an operator is also exempt from regulation of the basic service tier. *Id.*; *see* Order and Notice of Proposed Rulemaking in CS Docket No. 96-85, FCC 96-154, __ FCC Rcd __, ¶¶ 23-32 (1996).

[39] NCTA at 5-6; TCI Comments at 24-25; General Instrument Comments at 10-12; TIA Comments at 3-4.

[40] Section 623(b)(3) of the Communications Act.

[41] New Jersey Rate Advocate Comments at 5.

shall permit the associated equipment costs to be aggregated into a broad category.

B. Organizational Levels

14. *Background.* In the *Notice*, we proposed that Section 76.923(c) of our rules be amended to permit operators to aggregate equipment costs specifically at the franchise, system, regional, or company level.[42] Because our rules require equipment rates to be based on actual cost, we proposed amending our rules to require that equipment rates be set at the same level at which an operator chooses to aggregate its costs.[43] Furthermore, to the extent that our current rules permit cost aggregation of equipment only in a manner consistent with an operator's practices on April 3, 1993, we proposed eliminating that date restriction.[44] We tentatively concluded that such a restriction would improperly prevent an operator from aggregating costs at higher organizational levels, as specifically permitted in the statute.[45]

15. We also tentatively concluded that Congress did not intend that cost aggregation be permitted to the same extent for installation charges.[46] We reached this tentative conclusion because Section 301(j) of the 1996 Act refers only to equipment and not to installations, whereas the 1992 Cable Act separately mentions installations.[47] In the *Notice*, we stated that although customer equipment charges are not likely to vary significantly between systems, installation charges, which are more dependent on local labor costs, could vary between communities. To reduce burdens on cable operators, however, we proposed that operators be permitted to aggregate installation costs at higher geographical levels if the labor costs within that level were substantially similar.[48] Under this approach, we stated that an operator could establish installation rates for a specific service or geographical area, where the labor costs were substantially similar throughout all franchises in that area. We sought comment on our tentative conclusions, proposed rule amendments and sought comment on whether there were alternative levels at which installation costs could be identified that would ease burdens on operators, yet still comport with Congressional intent.[49]

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[42] *Notice*, __ FCC Rcd at __, ¶ 11.

[43] *Notice*, __ FCC Rcd at __, ¶ 11.

[44] *See* 47 C.F.R. § 76.923(c).

[45] *Notice*, __ FCC Rcd at __, ¶ 11.

[46] *Notice*, __ FCC Rcd at __, ¶ 12.

[47] *See* Communications Act, § 623(b)(3), 47 U.S.C. § 542(b)(3).

[48] *Notice*, __ FCC Rcd at __, ¶ 12.

[49] *Notice*, __ FCC Rcd at __, ¶ 12.

16. *Discussion.* No party disagreed with our tentative conclusion to eliminate the April 3, 1993 restriction. The 1996 Act requires cable operators to be permitted to aggregate equipment costs at the franchise, system, regional, or company level, regardless of their practices on April 3, 1993. In order to implement this Congressional intent, we therefore eliminate the April 3, 1993 date restriction for geographic averaging and amend our rules accordingly.

17. We amend Section 76.923(c) of our rules to permit operators to aggregate equipment costs specifically at the franchise, system, regional, or company level.[50] Upon further examination, we conclude that Congress intended that cable operators be permitted to aggregate installation costs at the same organizational level at which the operator aggregates its equipment costs. Furthermore, because our rules require equipment rates to be based on actual cost, we amend our rules to require that equipment and installation rates be set at the same level at which an operator chooses to aggregate its costs.

18. The New Jersey Rate Advocate stated that installation costs should not be aggregated at a multi-state level, but is not opposed to aggregation of installation costs at the state level.[51] In fact, the New Jersey Rate Advocate stated that in New Jersey, cable operators are permitted to aggregate installation costs at the same level as equipment costs.[52] The New York PSC agreed that cable operators should be permitted to aggregate installation costs at higher organizational levels where they can demonstrate that labor costs are substantially similar.[53] The remaining parties, NCTA, Time Warner, TCI, General Instrument and TIA, argued that in order to effectuate Congressional intent fully, cable operators should be permitted to aggregate installation costs at the same organizational level at which they choose to aggregate equipment costs.[54]

19. In the 1992 Cable Act, Congress included installation rates in the equipment rates subsection, directing the Commission to adopt standards to establish the price or rate for the installation and lease of equipment.[55] Upon reflection, we believe that because this provision refers to both the lease and installation of equipment, the most appropriate reading of the term "equipment," in both the 1992 Cable Act and the 1996 Act, is that it includes installation. This conclusion is also consistent with existing Commission regulations, which

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[50] *Notice*, __ FCC Rcd at __, ¶ 11.

[51] The New Jersey Rate Advocate Comments at 9.

[52] *Id.*

[53] New York PSC Comments at 4.

[54] NCTA Comments at 6-7; Time Warner Comments at 3-5; TCI Comments at 8-15; General Instrument Reply Comments at 5-7; and TIA Comments at 4.

[55] Communications Act of 1934, as amended, §623(b)(3).

include both equipment and installation costs in the Equipment Basket.[56] In addition, labor costs, required for maintenance and repair of the equipment, are an essential component of establishing subscriber equipment rates.[57]

20. Furthermore, the labor component of the Hourly Service Charge ("HSC") is used to calculate both equipment and installation rates.[58] Thus, as Time Warner and TCI note, limiting the level at which installation costs may be aggregated necessarily produces different HSCs, possibly hundreds for a large multiple system operator required to report installation costs at the franchise level.[59] Different HSCs will in turn produce different equipment rates and prevent an operator from establishing uniform rates for any of its customer equipment, thereby frustrating the actual cost standard.[60] For example, an operator that aggregates equipment costs at the company level might be forced to establish different equipment rates for each franchise area that it serves if it is unable to aggregate installation costs at the same organizational level.[61] This result would negate the intent of Congress to ease the regulatory burdens on cable operators in enacting this section of the 1996 Act. We therefore conclude that Congress intended that installation be subsumed under its general statutory reference to equipment and that the same cost aggregation rules should apply to both.[62]

21. Moreover, although we tentatively concluded in the *Notice* that labor costs might vary more significantly than equipment costs, we now conclude, as we had earlier for equipment costs, that any rate increases due to permitting installation cost aggregation at the same level of equipment cost aggregation will not be significant.[63] For example, in its comments TCI used its highest ($34) and lowest ($16) HSC to calculate a uniform HSC at the company level.[64] TCI then showed that use of the uniform HSC would only change converter

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[56] 47 C.F.R. § 76.923(c).

[57] *See, supra*, fn 12 and 13.

[58] *Id.*

[59] Time Warner Comments at 4-5; TCI Comments at 10-11.

[60] TCI Comments at 11.

[61] TCI Comments at 13.

[62] Time Warner and TCI argue for the conclusion we reach here. Time Warner Comments at 4; TCI Comments at 8-9.

[63] *See* TCI Comments at 13-15.

[64] *Id.*

prices an average of plus or minus $0.10.[65] Similarly, TCI showed that the use of the uniform HSC would, at most, increase the rate of an initial installation by approximately $4.50. For a typical TCI subscriber, who remains a customer for three years, this would produce an effective installation rate increase of approximately $0.15 per month.[66] Since these installation cost-aggregation-related price effects are identical to those associated with equipment cost aggregation, we conclude that, as Congress determined with equipment costs, the benefits of installation cost aggregation outweigh any adverse effects that may result. We also note that permitting installation cost aggregation will also result in rate decreases for many subscribers, and will be revenue-neutral for the cable operator. Finally, as Time Warner stresses, it is unreasonable to assume that Congress intended to streamline the rate regulation process and reduce regulatory burdens on cable operators by permitting equipment cost aggregation at one level, while simultaneously negating the benefits of such streamlining by requiring operators to aggregate installation costs at a different, lower level.[67] We agree and amend our rules accordingly.

C. Basic-Only Subscriber Equipment

22. *Background.* The 1996 Act prohibits "[s]uch aggregation . . . with respect to equipment used by subscribers who receive only a rate regulated basic service tier." In the *Notice*, we tentatively concluded that Congress was concerned that basic-only subscribers not bear the costs of more sophisticated equipment used by subscribers taking services in addition to basic.[68] We therefore tentatively concluded that equipment used by basic-only subscribers could not be aggregated into broad categories and could not be aggregated with equipment used by non-basic-only subscribers and proposed amending Section 76.923(c) of our rules to that effect.[69] We noted, however, that the statute is not clear as to whether a cable operator may aggregate the costs of equipment used by basic-only customers at higher organizational levels and develop system, regional, or company average prices for such equipment.[70] Although we recognized this ambiguity, we tentatively concluded that allowing cable companies to aggregate the costs of equipment used by basic-only subscribers at higher organizational levels and set rates at that same level would not contravene Congress' concern that basic-only subscribers not bear the costs of more sophisticated equipment used by

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[65] *Id.*

[66] *Id.*

[67] Time Warner Comments at 4.

[68] *Notice*, __ FCC Rcd at __, ¶ 13.

[69] *Notice*, __ FCC Rcd at __, ¶ 13.

[70] *Notice*, __ FCC Rcd at __, ¶ 13.

subscribers taking other services in addition to basic.[71] We sought comment on this issue.

23. *Discussion.* We conclude that Congress intended to ensure that basic-only subscribers not bear the costs of equipment used by subscribers taking services in addition to basic. Therefore, pursuant to the statutory language, costs of equipment used by basic-only subscribers may not be aggregated with costs of equipment used by non-basic-only subscribers. Furthermore, because we believe it furthers the goal of efficiency sought by Congress in this provision, without creating additional costs to the basic-only subscribers intended to be protected by it, we shall also permit an operator to aggregate costs of basic-only subscribers' equipment at the same organizational level at which the operator chooses to aggregate its other costs. We underscore, however, that such organizational aggregation must be within the basic-only subcategory. Because there is not always one type of equipment which may be deemed "basic-only equipment," we shall also permit an operator to aggregate costs of types of equipment used by non-basic-only subscribers with other non-basic-only equipment when setting rates for non-basic only subscribers, even if the same type of equipment is also used by basic-only subscribers.

24. The majority of parties filing comments in this proceeding agreed with our tentative conclusion that Congress intended that basic-only subscribers not bear the costs of equipment used by non-basic-only subscribers, which may be more advanced and expensive than basic-only subscriber equipment.[72] The majority of comments also agreed with our tentative conclusion to permit basic-only equipment costs to be aggregated at higher organizational levels.[73] The New Jersey Rate Advocate opposed cost aggregation of equipment used by basic-only subscribers at higher organizational levels, unless all franchise areas required the same customer equipment to receive basic service.[74] The New Jersey Rate Advocate also believes that even where that condition is met, cost aggregation should be limited to an intrastate level.[75] We believe that both of the New Jersey Rate Advocate's suggested limitations are contrary to the statutory language and Congressional intent. Other than the franchise level, any of the remaining three organizational levels explicitly listed by

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[71] *Notice*, __ FCC Rcd at __, ¶ 13.

[72] NCTA Comments at 8-9; TCI Comments at 20-22; General Instrument Reply Comments at 9-10; TIA Comments at 4; New York PSC at 3-4; New Jersey Rate Advocate Comments at 9. Time Warner argues that our tentative conclusion that Congress intended to prevent costs of equipment used by basic-only subscribers from being aggregated with costs of equipment used by non-basic-only subscribers represents an overly restrictive interpretation of the statutory language. Time Warner Comments at 5-7. Time Warner offers little justification for its statement and we believe there is no other reasonable interpretation of the statutory language.

[73] NCTA Comments at 8-9; TCI Comments at 20-22; General Instrument Reply Comments at 9-10;TIA Comments at 4; New York PSC at 3-4; and Time Warner Comments at 6.

[74] The New Jersey Rate Advocate Comments at 10.

[75] *Id.*

Congress could result in cost aggregation at levels above an intrastate level. There is no statutory basis to distinguish intrastate level and higher level aggregation. Adopting the New Jersey Rate Advocate's suggestions would therefore frustrate Congressional intent. Likewise, since we conclude that the prohibition against aggregation of equipment used by basic-only subscribers with equipment used by other subscribers applies to subscribers, not equipment, the New Jersey Rate Advocate's concern that all basic-only subscribers use the same equipment before cost aggregation at any organization level may occur is not relevant. We therefore believe that both our statutory interpretations are reasonable. In the 1996 Act, Congress explicitly stated that costs could be aggregated at the franchise, system, regional or company level.[76] We believe that allowing such aggregation for costs of equipment used by basic-only subscribers will not conflict with Congress' concern that basic-only subscribers not bear the costs of equipment used by non-basic-only subscribers. In fact, we believe that permitting operators to do so comports with Congress' intent to ease the regulatory burdens on operators.

25. TCI proposed an alternative approach for implementing the basic-only subscriber exception.[77] Under TCI's approach, an operator would be able to aggregate costs, at higher organizational levels, of equipment used by basic-only subscribers as detailed above, but with one difference. Instead of aggregating costs of equipment actually used by basic-only subscribers, TCI proposes to permit an operator to implement the basic-only subscriber exception on the assumption that all basic-only subscribers use equipment that is the lowest level and least expensive model of equipment offered by the operator, even if some basic-only subscribers actually have higher level, more expensive equipment.[78] TCI's approach would result in a rate decrease for basic-only subscribers in areas where basic-only and non-basic-only subscribers use the same equipment. No basic-only subscribers, however, would have a rate increase as a result of TCI's proposal. We believe TCI's approach complies with Section 301(j) of the 1996 Act and operators therefore retain the discretion to employ such an approach. In keeping with the flexibility Congress intended to exist in this area, however, we shall not require that operators employ TCI's approach.

D. FCC Form 1205 Review

26. *Background.* In the *Notice*, we stated that affected local franchising authorities would continue to review the equipment rates and supporting aggregated cost data as part of the review of the cable operators' rate justifications for the basic service tier.[79] We noted, however, that the review of aggregated equipment cost data by each affected local franchising

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[76] Communications Act, § 623(a)(7)(A), 47 U.S.C. § 543(a)(7)(A).

[77] TCI Comments at 16-20.

[78] *Id.*

[79] *Notice*, __ FCC Rcd at __, ¶ 14.

authority could lead to different review methods and inconsistent orders regarding the same data.[80] We therefore sought comment on alternative review proposals that might be more administratively efficient for local franchising authorities and cable operators alike.[81]

27. *Discussion.* We believe that our tentative conclusion that review of FCC Form 1205 should continue at the local franchise authority was correct. Therefore, local franchising authorities affected by the new cost aggregation rules established here will continue to review an operator's FCC Form 1205, with the operator retaining the right to appeal the local rate order to the Commission.

28. As an alternative review procedure, NCTA and Time Warner proposed that operators file their FCC Form 1205s directly with the Commission, which would then review the forms and determine the reasonableness of the averaging methodology used and the resulting rates.[82] Under the NCTA and Time Warner plan, local franchising authorities would retain the authority to enforce the rates resulting from the Commission's review and would also continue to set the basic service tier rate.[83] In support of their position, NCTA and Time Warner argue that the 1992 Cable Act left the precise level of local versus federal authority over equipment and installation rates to the Commission's discretion.[84] In addition, they note that the Commission has previously concluded that, in the social contract context, Commission review of aggregated equipment and installation costs and rates "does not violate any provision of the 1992 Cable Act."[85]

29. FCC Form 1205 has always contemplated higher than the franchise level cost aggregation in some circumstances and yet our rules have kept review of the form at the local franchising authority level. We are not aware of any problems with that aspect of the form, i.e., possible cost aggregation above the franchise level, but review at the franchise level. For example, no petitions for reconsideration were filed regarding that aspect of our original benchmark rate regulation rules. Furthermore, we have not received appeals from local rate

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[80] *Notice*, __ FCC Rcd at __, ¶ 14.

[81] *Notice*, __ FCC Rcd at __, ¶ 14.

[82] NCTA Comments at 9-13; Time Warner Comments at 8-9.

[83] *Id.*

[84] *Id.* In support of their argument, NCTA and Time Warner cite both Section 623(b)(3) of the Communications Act of 1934, as amended, which directs the Commission to prescribe cost-based regulations for equipment and installation separate from regulations for basic cable service and Section 623(b)(5) of the Communications Act of 1934, as amended, which grants the Commission exclusive authority to determine the "standards, guidelines and procedures concerning the implementation and enforcement" of the equipment rate regulations.

[85] Time Warner Social Contract at ¶¶ 37, 41; Continental Social Contract at ¶26.

orders asserting that inconsistent review of Form 1205 has occurred. Should we receive such appeals, we will act in accordance with our standard of review to correct misapplication of our rules.

30. Congress gave no indication in the 1996 Act that it sought to change the rules the Commission has adopted on the role of local franchising authorities in the review of FCC Forms 1205. Moreover, our decisions to accept Commission review of FCC Form 1205 in the context of social contracts were negotiated with individual operators and were not of general applicability. These contracts were made against the backdrop of rules which limited an operator's flexibility to aggregate equipment costs; rules that have been largely overridden by the 1996 Act. In fact, we specifically waived our rules to permit the companies that are parties to social contracts with the Commission to aggregate costs on a regional basis and to accept Commission review of those operators' Form 1205s.[86] We conclude that Congress, in passing the 1996 Act, did not seek to disturb the current procedure for review of an operator's Form 1205 at the local franchise level, a procedure that has been utilized since Form 1205's inception. Local franchising authorities shall continue to regulate basic service tier rates, including equipment rates contained in Form 1205, and operators shall retain the right to appeal those local rate orders to the Commission. Given that the revised rules adopted here are intended to provide for greater flexibility and administrative simplicity in the process of evaluating equipment costs, we believe that the use of aggregated cost filings should not result in delays or other disputes between franchising authorities and cable operators. To the extent that we find that these rules result in a significant number of appeals to the Commission, we will revisit the issue of jurisdiction for aggregated cost filings.

E. FCC Form 1205

31. *Background.* We noted that FCC Form 1205 would need modification because of our tentative conclusions and proposed rules changes detailed in the *Notice*.[87] We proposed revisions to FCC Form 1205 set out in Appendix B of the *Notice* and sought comment on these revisions.[88]

32. *Discussion.* We received no comments on our proposed revisions to FCC Form 1205 contained in Appendix B of the *Notice*. To the extent that our tentative conclusions are different from the ones adopted here, we modify our revisions accordingly.

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[86] Time Warner Social Contract at ¶¶ 37- 41; Continental Social Contract at ¶¶ 26-32.

[87] *Notice*, __ FCC Rcd at __, ¶ 15.

[88] *Notice*, __ FCC Rcd at __, ¶ 15.

IV. PROCEDURAL PROVISIONS

A. Final Regulatory Flexibility Analysis

33. Pursuant to the Regulatory Flexibility Act of 1980, Pub. L. No. 96-354, 94 Stat. 1164, 5 U.S.C. §§ 601-612 ("Regulatory Flexibility Act"), the Commission's final analysis with respect to this *Report and Order* is as follows.

34. *Need and purpose of this action.* The Commission, in compliance with Section 301(j) of the 1996 Act, Section 623(a)(7) of the Communications Act, pertaining to equipment cost aggregation, is required to issue revisions to the appropriate rules and forms necessary to implement this new section of the 1996 Act.

35. *Summary of issues raised by the public in response to the Initial Regulatory Flexibility Analysis.* There were no comments submitted in response to the Initial Regulatory Flexibility Analysis.

36. *Significant alternatives considered and rejected.* We did not receive comments analyzing the administrative burden of equipment cost aggregation pursuant to the Regulatory Flexibility Act. The Commission nonetheless has attempted to minimize such burdens and notes that equipment cost aggregation will substantially reduce regulatory burdens on cable operators.

B. Paperwork Reduction Act

37. *Final Paperwork Reduction Act of 1995 Analysis.* This *Report and Order* has been analyzed with respect to the Paperwork Reduction Act of 1995 and found to contain a modified information collection requirement on the public. Implementation of any modified information collection requirement will be subject to approval by the Office of Management and Budget as prescribed by the Act.

V. ORDERING CLAUSES

38. Accordingly, IT IS ORDERED, pursuant to Sections 4(i), 4(j) and 623(a) of the Communications Act of 1934, as amended, 47 U.S.C. §§ 154(i), 154(j) and 543, the rules, requirements and policies discussed in this Report and Order ARE ADOPTED and Sections 76.923(a), (c), (f), (g) and (m) of the Commission's rules, 47 C.F.R. §§ 76.923(a), (c), (f), (g) and (m), ARE AMENDED as set forth in Appendix B.

39. IT IS FURTHER ORDERED that the requirements and regulations established in this decision shall become effective upon approval by the Office of Management and Budget of the new information collection requirements adopted herein, but no sooner than 30 days after publication of this Report and Order in the Federal Register.

40. IT IS FURTHER ORDERED that the Secretary shall send a copy of this Report and Order, including the Final Regulatory Flexibility Analysis, to the Chief Counsel for Advocacy of the Small Business Administration in accordance with paragraph 603(a) of the Regulatory Flexibility Act, Pub. L. No. 96-354, 94 Stat. 1164, 5 U.S.C. §§ *et seq.* (1981).

FEDERAL COMMUNICATIONS COMMISSION

William F. Caton
Acting Secretary

APPENDIX A

Comments:

General Instrument Corporation
National Cable Television Association
New York State Department of Public Service
State of New Jersey, Department of the Treasury, Division of the Ratepayer Advocate
Tele-Communications, Inc.
Telecommunications Industry Association
Time Warner Cable

Reply Comments:

General Instrument Corporation
State of New Jersey, Department of the Treasury, Division of the Ratepayer Advocate
Telecommunications Industry Association

APPENDIX B

Title 47, Part 76 of the Code of Federal Regulations is proposed to be amended as follows:

1. The authority citation for Part 76 continues to read as follows:

AUTHORITY: 47 U.S.C. §§ 151, 152, 153, 154, 301, 302, 303, 303a, 307, 308, 309, 312, 315, 317, 325, 503, 521, 522, 531, 532, 533, 534, 535, 536, 537, 543, 544, 544a, 545, 548, 552, 554, 556, 558, 560, 561, 571, 572, 573.

2. Section 76.923 is amended by revising paragraphs (a), (c), (f), (g) and (m), and revising it to read as follows:

§ 76.923 Rates for equipment and installation used to receive the basic service tier.

(a) *Scope.* The equipment regulated under this section consists of all equipment in a subscriber's home, provided and maintained by the operator, that is used to receive the basic service tier, regardless of whether such equipment is additionally used to receive other tiers of regulated programming service and/or unregulated service. Such equipment shall include, but is not limited to:

(1) Converter boxes;

(2) Remote control units; and

(3) Inside wiring.

Subscriber charges for such equipment shall not exceed charges based on actual costs in accordance with the requirements set forth below.

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(c) *Equipment basket.* A cable operator shall establish an Equipment Basket, which shall include all costs associated with providing customer equipment and installation under this section. Equipment Basket costs shall be limited to the direct and indirect material and labor costs of providing, leasing, installing, repairing, and servicing customer equipment, as determined in accordance with the cost accounting and cost allocation requirements of § 76.924, except that operators do not have to aggregate costs in a manner consistent with the accounting practices of the operator on April 3, 1993. The Equipment Basket shall not include general administrative overhead including marketing expenses. The Equipment Basket

shall include a reasonable profit.

(1) *Customer Equipment.* Costs of customer equipment included in the Equipment Basket may be aggregated, on a franchise, system, regional, or company level, into broad categories. Except to the extent indicated in subparagraph (2) below, such categorization may be made, provided that each category includes only equipment of the same type, regardless of the levels of functionality of the equipment within each such broad category. When submitting its equipment costs based on average charges, the cable operator must provide a general description of the averaging methodology employed and a justification that its averaging methodology produces reasonable equipment rates. Equipment rates should be set at the same organizational level at which an operator aggregates its costs.

(2) *Basic Service Tier Only Equipment.* Costs of customer equipment used by basic-only subscribers may not be aggregated with the costs of equipment used by non-basic-only subscribers. Costs of customer equipment used by basic-only subscribers may, however, be aggregated, consistent with an operator's aggregation under subparagraph (1) above, on a franchise, system, regional, or company level. Alternatively, operators may base its basic-only subscriber cost aggregation on the assumption that all basic-only subscribers use equipment that is the lowest level and least expensive model of equipment offered by the operator, even if some basic-only subscribers actually have higher level, more expensive equipment.

(3) *Installation Costs.* Installation costs, consistent with an operator's aggregation under subparagraph (1) above, may be aggregated, on a franchise, system, regional, or company level. When submitting its installation costs based on average charges, the cable operator must provide a general description of the averaging methodology employed and a justification that its averaging methodology produces reasonable equipment rates. Installation rates should be set at the same organizational level at which an operator aggregates its costs.

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(f) *Remote charges.* Monthly charges for rental of a remote control unit shall consist of the average annual unit purchase cost of remotes leased, including acquisition price and incidental costs such as sales tax, financing and storage up to the time it is provided to the customer, added to the product of the HSC times the average number of hours annually repairing or servicing a remote, divided by 12 to determine the monthly lease rate for a remote according to the following formula:

$$\text{Monthly Charge} = \frac{\text{UCE}+(\text{HSC} \times \text{HR})}{12}$$

Where, HR = average hours repair per year; and UCE = average annual unit cost of remote.

(g) *Other equipment charges.* The monthly charge for rental of converter boxes and other customer equipment shall be calculated in the same manner as for remote control units. Separate charges may be established for each category of other customer equipment.

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(m) Cable operators shall set charges for equipment and installations to recover Equipment Basket costs. Such charges shall be set, consistent with the level at which Equipment Basket costs are aggregated as provided in § 76.923(c). Cable operators shall maintain adequate documentation to demonstrate that charges for the sale and lease of equipment and for installations have been developed in accordance with the rules set forth in this section.

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